The SA Bullion Gold Report

First Quarter 2016

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Table 1: Gold Performance to 31 March 2016 (% per annum)[1]

	Quarter[2]	1 Yr	2 Yr	3 Yr	5 Yr	10 Yr
Gold in US Dollar	15.8	4.2	-2.1	-8.2	-3.0	7.8
Gold in Rand	12.6	29.2	15.6	7.2	13.6	17.7
Gold in Euro	10.8	-1.9	7.6	-4.5	1.3	8.5

[1] Based on LBMA Afternoon Fixes
[2] not annualized for periods of less than 1 year

Table 2: Quarter-End Gold Prices and Exchange Rates[1]

	Gold in $/oz	R/$ rate	Gold in R/oz[2]	$/€ rate	Gold in €/oz
31 March 2006	582.00	6.16	3,587.74	1.21	480.11
31 March 2007	661.75	7.25	4,799.34	1.33	496.70
31 March 2008	933.50	8.13	7,586.09	1.58	589.59
31 March 2009	916.50	9.86	9,032.22	1.33	688.99
31 March 2010	1,115.50	7.31	8,154.49	1.35	825.07
31 March 2011	1,439.00	6.75	9,717.63	1.42	1,014.52
31 March 2012	1,662.50	7.68	12,776.01	1.33	1,246.63
31 March 2013	1,598.25	9.32	14,902.44	1.28	1,245.90
31 March 2014	1,291.75	10.57	13,737.29	1.38	936.59
31 March 2015	1,187.00	11.96	14,194.58	1.07	1,106.22
31 March 2016	1,237.00	14.83	18,345.95	1.14	1,084.85

Note 1: Gold prices in US$ and € are LBMA Afternoon Fix prices
Note 2: Gold price in Rand from Rand Refinery

Table 3: Calendar Year Performance of Gold

	% US Dollar	% ZA Rand	% Euro
2006	23.2	37.0	10.2
2007	31.9	27.9	18.9
2008	4.3	41.1	9.7
2009	25.0	-0.4	21.1
2010	29.2	16.1	38.2
2011	8.9	33.0	12.6
2012	8.3	13.6	6.2
2013	-27.3	-11.8	-30.3
2014	0.1	10.4	13.4
2015	-11.4	19.1	-1.1
2016 year-to-date	15.8	12.6	10.8

Figure 1: Ten-Year Chart of Gold Price in US Dollar [LBMA PM Fix]

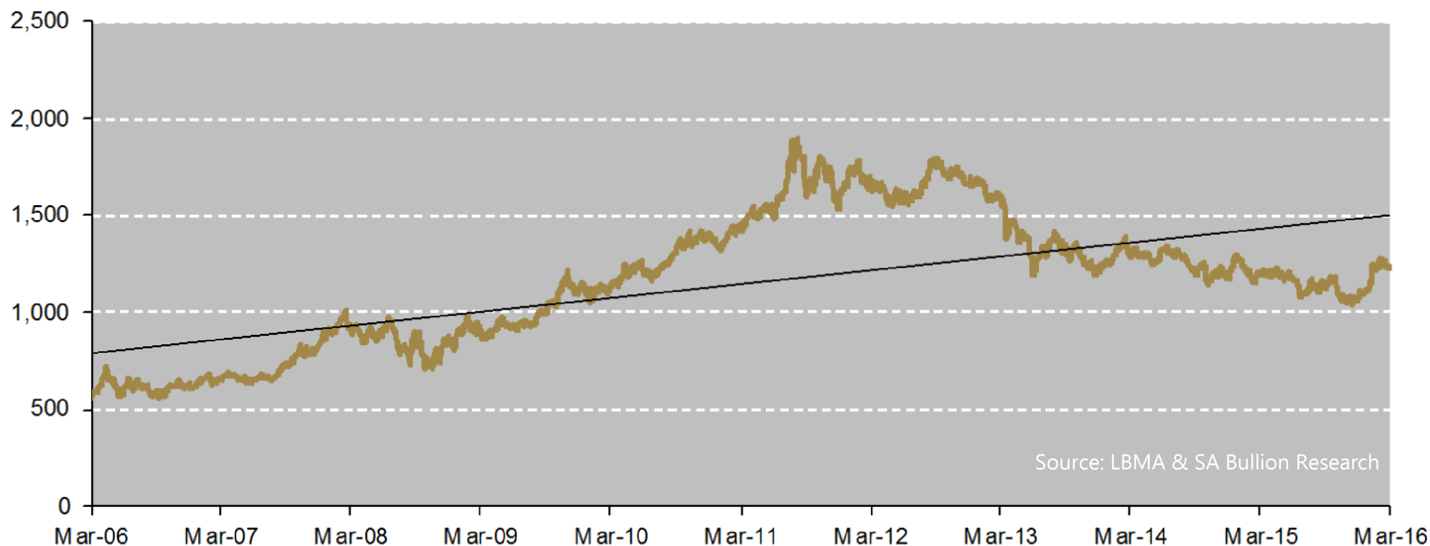
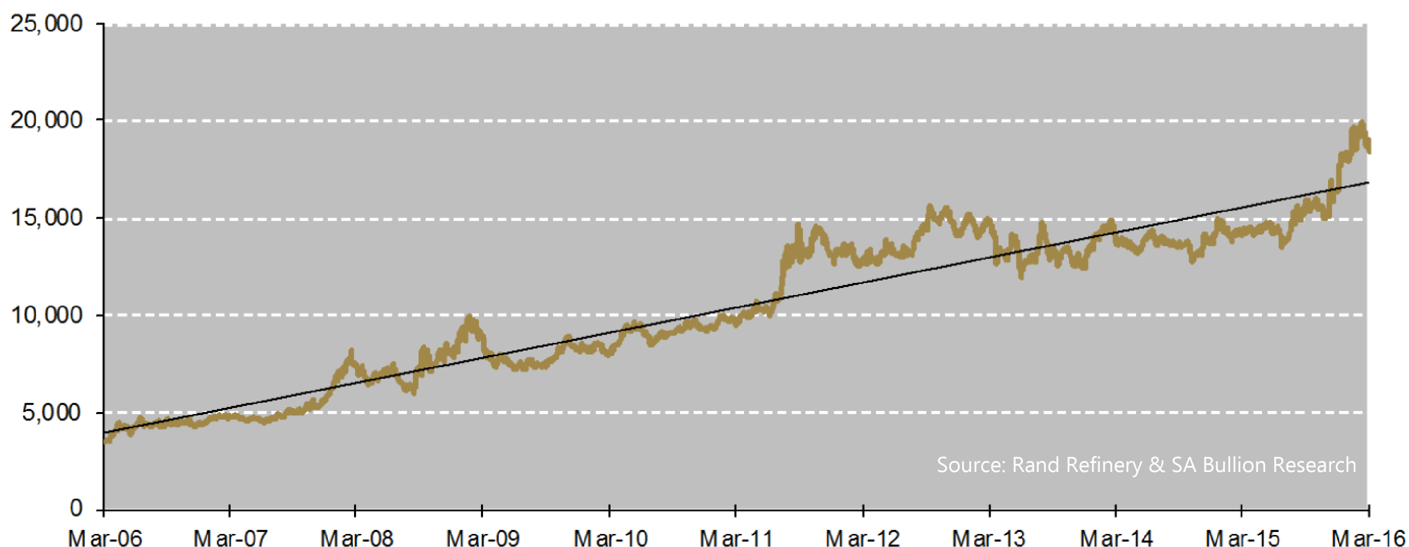


Figure 2: Ten-Year Chart of Gold Price in South African Rand (Rand Refinery First Pricing)



Gold Price Action

Gold produced excellent returns in the first quarter of 2016. Gold bullion began the quarter at R16,298.82 per ounce and ended it at R18,345.95 to return 12.6% for the three-month period. In US Dollar, the comparative figures are $1,068.25 to $1,237.00 to return 15.8%. These figures follow on from a year (2015) where gold returned 19.1% in Rand. To say that our Rand and Dollar clients have been happy investors in gold in recent times would be an understatement.

Over the last ten years, from 31 March 2006 to 31 March 2016, holders of gold have been extremely well rewarded. In US Dollar the annualized rate of return has been 7.8% and in South African Rand it has been 17.7%. Our thesis is that gold is a currency and therefore a competitor to cash in the bank. Furthermore, that gold should be held as a currency diversifier. Our position remains unchanged.

Global Review

We live in absurd times. These are times of economic stagnation and policy missteps. In her Spring Global Policy Agenda the managing director of the IMF paints a sorry picture of the global economy. Ms Lagarde has the view that the global economic outlook has weakened and that the risks have increased. She said: "growth is being dragged down by persistently high unemployment, high debt, and low investment in some countries, in addition to a long-term decline in productivity growth that predates the crisis".

At much the same time as the IMF boss was making pronouncements, so too was the US Federal Reserve Board (the "Fed") doing so. Ms Yellen indicated that the US, along with the rest of the world, runs the risk of ending up in a recession before too long. Now it must be mentioned that normally to emerge from a recession rates have to be cut by approximately four percentage points. However, we live in a world of extremely low interest rates and cutting by four percentage points from these low levels would be not just unthinkable but downright dangerous. The Effective Fed Funds Rate is currently about 0.36% (and the long bond rate is approximately 1.9%). How does one make significant cuts to a rate that is already so low? Of course rates have been taken into negative territory in recent times. Note these rates:

Table 4

Central Bank	Interest Rate (% p.a.)
Denmark Central Bank	-0.65
Sweden Central Bank	-1.10
European Central Bank	-0.30
Swiss National Bank	-0.75
Bank of Japan	-0.10

But we would point out that these extremely low or negative rates do not stimulate aggregate demand, and therefore economic growth, in periods of high leverage. They rather steer borrowings into financial assets which then serves to distort markets and currencies.

The global economy is plagued by excessive debt. In Germany, France, Italy, UK, US and Japan the combination of government debt and private sector debt ranges between 150% and 420% of GDP. The US figure is well over 300%. In order to keep going (without an enormous economic retrenchment), interest rates have to remain close to 0% or be in fact in negative territory so as to stimulate borrowing, and debts have to be allowed to continue to soar to ever higher levels.

Of course this situation is completely unsustainable. Of this one can be certain. Except with one possibility. In this one and only alternative case central banks would achieve the stimulation of inflation to reasonably high levels so that debts would be paid down in depreciated currency and central banks would have some room to cut rates (from newly hiked levels) in times of recession without taking rates into highly negative real-rate territory.

It has long been our belief that the escape hatch for regulators is inflation, which is a synonym for currency debasement. It is for this reason that we don't like fiat currencies but rather favour the one physically-backed currency – gold.

The US - overburdened with Debt

Even accounting for the disastrous and costly misadventures of President George W Bush, US national debt increased in the 17 years from 1990 to 2007 by an annual average of "just" $196.5 billion per year.

The great financial crisis of recent times began in late 2008 and in its essence, took five years to stabilize. During this period of madness, from 2008 to 2012, US national debt increased by a staggering average of $1,354.7 billion per year.

In the three full years post-stabilization, i.e. 2013 to 2015, one would have reasonably expected national debt expansion to have reduced to pre-crisis levels. One would also reasonably have expected economic growth (as measured by Gross Domestic Product, or 'GDP') to have picked-up to pre-crisis expansion rates given the levels of extraordinary monetary and fiscal stimulus of those five years of intervention madness. The story is otherwise.

In the three years of 2013 to 2015 US national debt increased at an average of $772.6 billion per year!

By the end of 2015 US national debt stood at $ 18.9 trillion and on 29 January of this year, US national debt surpassed $19 trillion for the first time in history. At quarter-end this figure was $19.3 trillion.

Of course the growth in size of the US national debt must be seen relative to the changing size of the debtor. In this case we look at the growth of the US economy as measured by growth in GDP. Given our comments in prior paragraphs regarding governmental stimulus, one would expect that the five year stabilization period would show poor GDP growth rates. This is so:

Table 5

Year	GDP growth (% p.a.)
2008	-0.3
2009	-2.8
2010	2.5
2011	1.6
2012	2.2

One would also expect a return to pre-crisis levels of GDP growth at around 5% p.a. in the period following stabilization and when government was still pumping the economy with debt averaging a pretty phenomenal $772 billion per year. This is not so:

Table 6

Year	GDP growth (% p.a.)
2013	1.5
2014	2.4
2015	2.4

The debtor was not responding very well to exceptional treatment. Given the levels of stimulus growth should have been astonishing, but was dismal. Of great interest also is the micro picture. The most recent four quarters of GDP growth appears thus:

Table 7

Quarter	GDP growth (% annualised)
Q2 2015	3.9
Q3 2015	2.0
Q4 2015	1.4
Q1 2016	0.5

What we are witnessing is economic stagnation. The US economy shows all the signs of being fundamentally sick and is rapidly running out of what little impetus it had. (If I were a betting man I would bet that the next president of the US is going to walk into a recession!) Bear in mind that the above figures don't portray the whole sad story – it gets worse. The population of the US continues to increase at around 0.8% per annum therefore GDP must expand by 0.8% per annum to stand still at a per capita rate. It goes without saying that GDP growth per capita is awful.

To come at this story from a different angle, I would like to take you, dear reader, back to some of our earlier writings. We posited that at a certain level of indebtedness the US would experience a braking effect brought to bear on its economic performance by way of increasing long term interest rates. We quoted IMF research that found that beyond a PDR (Public Debt Ratio) of 50%, there is a strong transmission of retardation to the economy. It is noteworthy that the US national debt (or 'public debt') by the end of 2012 had grown to $16.4 trillion while the economy had grown to only $16.2 trillion; and for the first time since the Second World War US national debt exceeded the size of the economy. The PDR therefore breached 100%. As at 31 March 2016 the figure is 106.6%! The IMF research indicates that for each percentage point in PDR that exceeds 50%, the effect is to increase long term interest rates by 5 basis points. With the PDR at 106.6% this IMF formula would indicate that long term rates will experience an additional elevation of 2.8 percentage points caused by the drag that comes with high levels of national debt. This effect on the economy of the US portents to be massive.

Post-2008 it has constantly been our view that the administering of more debt to the patient that had become sick due to too much debt in the first place, was not going to work and that economic stagnation would result and combined with monetary inflation, stagflation would be the outcome. We think the chickens are coming home to roost and gold is the currency of choice in such economic circumstances.

SA Bullion news

In this our tenth year of existence we are developing, expanding and improving on all fronts. We have gone through a process of self-analysis and determined that we can make improvements to our brand and market positioning. In this regard we will be coming to you with some exciting developments shortly.

In the Human Capital area we are extremely pleased to announce that we have hired Adnaan Bazier as Business Development Manager. Adnaan has B Com and MBA degrees as well as numerous other prestigious qualifications. I feel rather pleased that he worked at Allan Gray in the unit trust company that I established in my days at the same firm and that he comes highly recommended. Adnaan joined the team in mid-April and has already become a highly valued member of the management team. We have exciting times ahead!

In closing, I would like to thank you for your support in our first ten years. It has been most exciting and gratifying. I look forward to thanking you when we get to twenty!

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